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Memorandum for: DDI

The attached was sent today to Peter
Sommer, NSC, for his background use.

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Chief, Western Europe Division
Office of European Analysis

27 October 1983



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**Office of European Analysis
Directorate of Intelligence**

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Memorandum for: Mr. Peter R. Sommer
National Security Council
European and Soviet Affairs Staff

SUBJECT: Background and Implications of the DM
One Billion West German Credit to East
Germany

1. Per your request last week, attached is
a short paper on the above subject [redacted]
[redacted] basic judgments are that Bonn and
East Berlin both see the loan as mutually
beneficial; [redacted]

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[redacted] and both sides are
leaning toward another loan, although Warsaw
Pact reaction to INF deployments may delay
signature.

2. If we can be of any further assistance,
please call John McLaughlin [redacted]
[redacted]

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Chief, Western Europe Division
Office of European Analysis

26 October 1983



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**Office of European Analysis
Directorate of Intelligence**

26 October 1983

MEMORANDUM

West Germany - East Germany: Background and Implications
of the DM One Billion Credit

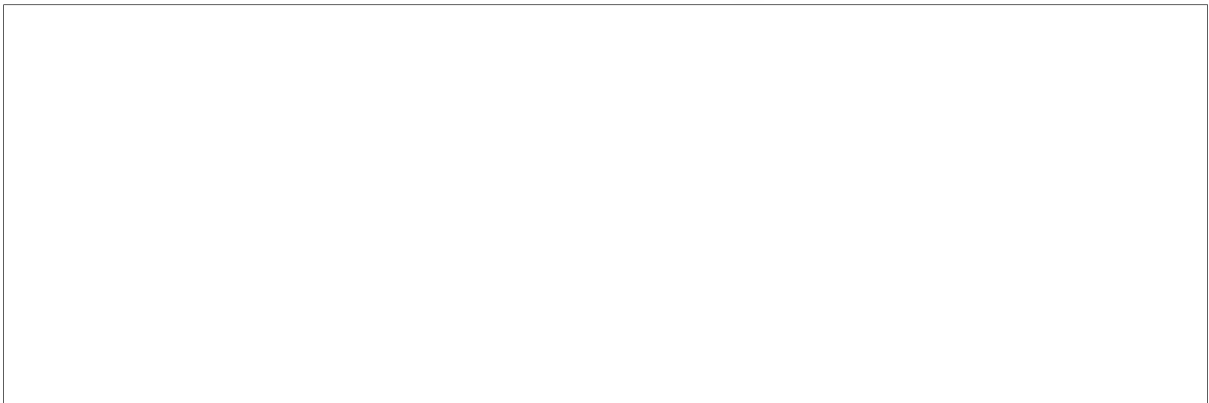
The one billion deutsche mark (DM) (US \$400 million) financial credit to East Germany announced 29 June 1983 was arranged by a consortium of West German banks led by the Bayerische Landesbank. The loan carries a commercial interest rate of one percentage point over Libor (currently 5.8 percent for Euro-DM) and is repayable in five years. The credit is guaranteed by the West German government with Bonn's annual transit and postal payments to East Germany -- DM 610 million (US \$245 million) -- reportedly serving as collateral. We doubt that this guarantee is as "costless" as Bonn has portrayed it, however. Should the East Germans fall in arrears in repaying the loan, this would signify serious financial problems; in this case, the current government in Bonn might be unwilling to exacerbate these problems by withholding fees to the East Germans. [REDACTED]

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The considerable controversy in West Germany over the credit stems from several factors.

- o It is the first untied financial credit West Germany has ever provided East Germany. In the past only much smaller credits tied to specific deliveries have been granted.

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In September, East Germany announced minor moves undoubtedly intended to be seen as concessions for the credit. New applications for family reunification and marriage with foreigners could be expected to be "duly processed and treated with goodwill," automatic firing devices were to be removed from border areas, and the minimum currency exchange requirement for Western visitors* was to be waived for children under 14. West German Chancellery officials welcomed the concessions as a first step but say more is required. [REDACTED]

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Since the announcement of the West German credit, Western bankers have shown a marginally improved willingness to resume lending to East Germany. West German bankers have been the most positive. [REDACTED]

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Background to the Loan

In early 1982, East Germany had reached the limit of its ability to borrow internationally, and some Western banks were withdrawing credit lines because of East Germany's precarious financial position. [REDACTED]

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*The minimum daily exchange was DM 6.50 for Western visitors to East Berlin and DM 13 for visitors to East Germany. Retired people and children under 15 were exempt. In October 1980, East Germany increased the rate to a uniform DM 25 and imposed a rate of DM 7.50 for children under 15. [REDACTED]

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West German Political Motivation

The Kohl government probably had a mixture of motives for guaranteeing the loan. Externally, the agreement aims at promoting contact between East and West Germans, sheltering intra-German relations from any East-West chill that follows INF deployments, and showing the East German and Soviet governments that the new conservative government in Bonn is able and willing to cooperate with them usefully. Kohl made clear when he assumed power in October 1982 that his government would honor the Eastern treaties arranged by the Brandt government in the early 1970s and would seek to advance relations with the countries of the Soviet Bloc, especially for the sake of promoting contacts between the people of the two Germanies. Although his party had fought the treaties a decade earlier, by 1982 Kohl realized that Ostpolitik had the broad acceptance of the West German public. As Chancellor, he has sought to demonstrate that his conservative administration, while emphasizing unequivocally its commitments to the West, could still maintain a dialogue with the Soviet and East German leaders. [REDACTED]

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The East German Side

For East Germany, the loan was advantageous both politically and economically. Economically, the repayment time and the interest rate were much better than any other commercial financing available to East Berlin since 1980. The lack of any specific tie to imports or particular projects also left East Germany free to use the proceeds to improve the maturity structure of its debt, thus helping to stave off any need to reschedule. [REDACTED]

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Politically, the loan coincided with a push by East Berlin to show Bonn the possibilities of intra-German relations. Since the loan announcement, the number of Bonn politicians visiting East Berlin has dramatically increased, and East German officials are indicating that several dormant bilateral negotiations could be advanced. Most of these moves have been of low cost to East Germany, however, reflecting mixed motives -- East German leader Honecker recently warned of the possibility of an intra-German "ice age" if INF deployment proceeds. East Berlin would much prefer to weather any chill in East-West relations without sacrificing further hard currency flows from Bonn, but it probably is prepared to sacrifice some of the recent ostensible improvements in intra-German relations for the sake of Warsaw Pact unity.

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A Second Loan?

Despite rumors of a second loan of DM 3-4 billion (US \$1.2-\$1.6 million), West German government officials and bankers say they have received no official East German request. West German Chancellery officials indicate they are not opposed in principle to another loan if East German concessions can be nailed down in advance.

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